# German, Italy Economies Shrank at Record Pace in First Quarter

By Jana Randow

May 15 (Bloomberg) -- The German and Italian economies contracted more than forecast in the first quarter, slumping the most on record after the global financial crisis crippled exports and investment across Europe.

German gross domestic product plunged a seasonally adjusted 3.8 percent from the fourth quarter, when it fell 2.2 percent, the Federal Statistics Office in Wiesbaden said today. That's the steepest drop since quarterly data were first compiled in 1970 and compares with the 3 percent decline predicted by economists in a Bloomberg News survey. Italian GDP fell 2.4 percent, the most since records began in 1980, and France's economy shrank 1.2 percent.

Chancellor Angela Merkel's government, which predicts the economy will contract 6 percent this year, is spending 82 billion euros ($112 billion) to haul Germany out of its worst recession since World War II. Some indicators have shown first signs of stabilization, with manufacturing orders rising for the first time in seven months in March and business confidence rebounding from a 26-year low in April.

Today's report "was dramatically worse than expected," said Joerg Lueschow, an economist at WestLB in Duesseldorf. "We can only hope that the improvement in sentiment wasn't a mirage but a sign of stabilization and recovery."

The euro fell more than half a cent to $1.3576.

'Slow and Protracted'

While policy makers have expressed optimism that the world recession may be easing, any recovery is likely to be slow. The global economy will shrink 1.3 percent this year and only return to growth in 2010, the International Monetary Fund says.

Bank of England Governor Mervyn King said on May 13 the U.K.'s recovery will be "slow and protracted." In the U.S., rising unemployment may restrain consumer spending, the biggest part of the economy. Japan will next week say its economy shrank a record 4.3 percent in the first quarter from the fourth, a survey of economists shows.

Germany's first-quarter slump, which marked an unprecedented fourth successive quarterly contraction, was led by a decline in exports and investment, the statistics office said. Consumer and government spending rose "slightly" in the quarter. In the year, the economy shrank 6.9 percent when adjusted for the number of working days.

"The main pillars of the economy have continued to weaken," said Stefan Bielmeier, an economist at Deutsche Bank AG in Frankfurt. "It could mean that GDP will be weaker than expected in other countries. The risk for euro-region GDP figures is pointing significantly downward."

'Great Recession'

Spain's economy contracted 1.8 percent in the first three months of the year, the country's statistics office said yesterday. Italy will report GDP at 10 a.m. and Eurostat, the European Union's statistics arm in Luxembourg, publishes first- quarter data for the entire 16-nation euro region at 11 a.m. Economists forecast a 2 percent contraction.

"The latest ugly GDP figures should mark the trough of the current 'Great Recession'," said Alexander Koch, an economist at UniCredit in Munich. "Business sentiment in Germany and almost all other major economies has found a floor recently."

European confidence in the economic outlook increased for the first time in 11 months in April and the recession in the region's manufacturing industry eased for a second month. German exports unexpectedly rose in March and industrial production held steady, ending a six-month slump and adding to signs that the worst may be over.

Grounds For Optimism

"I believe there are some grounds for being optimistic that the pace of decline in economic activity will decelerate markedly in the months ahead," Bundesbank President Axel Weber said this week. "However, it is certainly not advisable to be overly optimistic that the recovery process is safely on track. This will most likely be a gradual process."

Siemens Chief Executive Officer Peter Loescher said on April 29 he sees no sign of the economic recovery needed to spur manufacturing demand. Orders declined 11 percent to 20.9 billion euros in the first three months of the year. Europe’s largest engineering company reported a bigger-than-expected jump in earnings after accelerating its cost-cutting program.

Linde AG, the world’s second-biggest maker of industrial gases, said on May 5 it will cut about 3,000 jobs this year and it’s no longer counting on increasing 2009 profit and sales. At BASF SE, the world’s biggest chemical company, job cuts are being extended to 2,000 and a total 7,000 workers are being put on shorter hours.

Rising Unemployment

German unemployment rose for a sixth straight month in April, pushing the jobless rate to a 16-month high of 8.3 percent.

The European Central Bank cut its benchmark interest rate to a record-low 1 percent last week and said that’s not necessarily its lowest level. President Jean-Claude Trichet also announced the ECB will buy 60 billion euros of covered bonds, securities backed by mortgages and public-sector loans, in an attempt to free up credit.

The IMF expects the euro-area economy to shrink 4.2 percent this year and 0.4 percent in 2010.

“It will probably take several years before we completely make up for the contraction of the past quarters,” said Simon Junker, an economist at Commerzbank AG in Frankfurt. “We tend to reach for signs of hope. They’re there, but that doesn’t mean that we’ll immediately begin to grow strongly.”

The statistics office revised the fourth-quarter contraction to 2.2 percent from 2.1 percent. It will publish a detailed breakdown for the first quarter on May 26.

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